

Daniel P. Collins

UNITED STATES BANKRUPTCY COURT

In re:) Chapter 13 Proceedings
)
MICHAEL GORDON HALSAM,) Case No.: 2:14-bk-15861-DPC
)
Debtor.) Adversary No. 2:15-ap-00068-DPC
)
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MAYO CLINIC,) UNDER ADVISEMENT ORDER
)
Plaintiff,)
)
v.)
)
MICHAEL GORDON HALSAM,)
)
Defendant.)

Mayo Clinic (“Plaintiff”) filed this adversary proceeding seeking a judgment of this Court holding Plaintiff’s claims against Michael Halsam (“Debtor”) nondischargeable under 11 U.S.C. § 523(a)(4)¹. For the reasons stated below, the Court holds that Plaintiff’s claim is nondischargeable in this Chapter 13 proceeding.

I. Procedural History

A. State Court Proceedings

On December 21, 2012, Plaintiff filed a lawsuit against Debtor in the Arizona Superior Court, Maricopa County (CV2012-018484) (“State Court Action”) claiming breach of contract, conversion, fraud, and unjust enrichment. Plaintiff sought damages in the amount of \$199,557.02 claimed owing to Plaintiff for healthcare services provided by

¹ Unless otherwise indicated, all Chapter, Section, and Rule references are to the Bankruptcy Code (“Code”), 11 U.S.C. §§ 101-1532 and to the Federal Rules of Bankruptcy Procedure, Rules 1001-9037.

1 Plaintiff to Debtor (See Adversary Proceeding Docket Entry (“DE”) 47 and Trial Exhibit
2 (“Ex”) 5). Plaintiff claimed Debtor assigned insurance proceeds to Plaintiff but that
3 Debtor retained \$155,304.86 paid directly to him by Blue Cross Blue Shield (“BCBS”)
4 (Ex 5). Plaintiff claimed Debtor’s retention of these insurance proceeds constituted a
5 conversion of those funds and fraud under Arizona’s Uniform Fraudulent Transfers Act
6 (Ex 5). Plaintiff moved for summary judgment in the State Court Action. On September
7 17, 2014, the Superior Court granted Plaintiff’s Motion, stating:

8 In this Case, the Court finds that there are no material facts in dispute.
9 Defendant was a patient at the Mayo Clinic and received treatment.
10 Defendant owes Mayo Clinic for those services. Defendant received directly
11 from his insurance provider over \$155,000.00 and instead of paying Mayo
12 Clinic as agreed, Defendant simply pocketed the money. Defendant claims
13 that he was overcharged and/or that he had an agreement to pay less. The
14 Court finds that no such facts were presented and that no such agreement
15 existed and that Defendant owes the full amount.

16 (See Plaintiff’s Motion for Summary Judgment (DEs 22-25) and Exhibit M attached to
17 DE 25).

18 During Plaintiff’s State Court Action against Debtor, Debtor claimed in his answer
19 (Ex 6, ¶ 8) that Plaintiff was not deprived of funds to which it was entitled. In his
20 subsequent discovery responses Debtor claims he had not spent or otherwise utilized the
21 \$155,305.86 of insurance proceeds sent to him by BCBS (Ex 3, ¶ 6).

22 B. Bankruptcy Proceedings

23 On October 21, 2014, Debtor filed this bankruptcy. On January 30, 2015, Plaintiff
24 brought this adversary proceeding seeking a judgment of this Court finding Debtor’s
25 obligations to Plaintiff nondischargeable under 11 U.S.C. §§ 523(a)(2)(A) and (a)(4) (DE
26 1). On March, 30, 2015, Debtor filed his Answer and Counterclaim (DE 6) but later
acknowledged his counterclaims were barred by applicable statutes of limitation and
should be dismissed (DE 39). On January 29, 2016, Plaintiff filed a motion for summary
judgment (DE 22-25). Debtor objected claiming that, while he owed money to Plaintiff,

1 that obligation was dischargeable because (1) his insurance assignment to Plaintiff was
2 not absolute, (2) he owned the insurance proceeds when he received them, and (3) there
3 are no circumstances indicating fraud in connection with Debtor's debtor-creditor
4 relationship with Plaintiff (DE 30-32).

5 The Court denied Plaintiff's motion for summary judgment, but found Plaintiff
6 satisfied two of the three factors established by the 9th Circuit B.A.P. in *In re Wada*, 210
7 B.R. 572 (9th Cir. BAP 1997) to prove embezzlement under 11 U.S.C. § 523(a)(4).
8 (DE 44). The Court found the *Wada* factors satisfied were: (1) the property was rightfully
9 in possession of a non-owner, and (2) the non-owner appropriated the property to a use
10 other than which he was entrusted (DE 44). The Court determined it could not resolve the
11 third *Wada* factor (circumstances indicating fraud) without conducting a trial on that
12 element of the embezzlement claim.

13 The parties filed their Joint Pretrial Statement on June 13, 2016 (DE 47). The Court
14 held a trial on June 20, 2016, and subsequently took this matter under advisement on June
15 20, 2016 (DE 48). At trial, Plaintiff withdrew its § 523(a)(2)(A) claims (Count I), as well
16 as that portion of § 523(a)(4) pertaining to "fraud or defalcation" while acting in a
17 fiduciary capacity (Count II).

18 **II. Stipulated Facts and Facts Not Contested at Trial**

19 Debtor is a single man who is in private practice as a chiropractor (DE 48). He
20 received medical care from Plaintiff on or about September 30, 2011 through Dec 30,
21 2011 for heart related issues. (DE 47, ¶ 1 and DE 48.) As a prerequisite to receiving
22 health care goods and services, Debtor signed an Authorization and Services Terms
23 Agreement ("ASTA"), the terms of which assign to Plaintiff any health insurance benefits
24 he was entitled to for the health care he received from Plaintiff. (Ex 2.) Under the ASTA,
25 Debtor also promised to immediately forward to Plaintiff all health insurance payments
26 he received for the services provided to him by Plaintiff (Id.) The total expense of the

1 healthcare services provided to Debtor by Plaintiff was \$199,557.02 (DE 47, ¶ 2). BCBS
2 provided Debtor \$155,305.02 to pay towards this bill (DE 47, ¶¶ 4 and 5).

3 **III. The Trial**

4 In his testimony at trial, Debtor admitted to being familiar with the type of
5 insurance arrangement described in the ASTA due to his experience as a healthcare
6 professional (DE 48). He also admitted at trial that he used the insurance money received
7 from BCBS for his own personal and business expenses, but that he planned to eventually
8 pay it back to Plaintiff (DE 48).

9 Contrary to Debtor's responses in the State Court Action, his discovery responses
10 in this bankruptcy indicate that he had deposited, transferred, and spent the entirety of the
11 insurance proceeds by August 2012 (Ex 4, ¶ 6). This was six months before Debtor's
12 answer in the State Court Action and almost one year before Debtor's discovery responses
13 in the State Court Action. Debtor claimed to have spent the money because he was deep
14 in personal and business debt because he was supporting himself, his girlfriend, and her
15 children (DE 48). Debtor testified that he intended to eventually pay the BCBS insurance
16 proceeds to Plaintiff (DE 48).

17 Plaintiff claims that circumstances indicating fraud exist and that Plaintiff is
18 entitled to a nondischargeable judgment for \$149,953.15 of the \$155,304.86 of insurance
19 proceeds paid directly to Debtor by BCBS (DE 47, ¶ 7).

20 **IV. Issue**

21 Did Debtor have the requisite intent to support a finding by this Court that there
22 were circumstances indicating fraud in connection with Debtor's relationship with
23 Plaintiff?

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26 **V. Analysis**

1 A. Burden of Proof

2 As with all actions under § 523, Plaintiff bears the burden of proof by a
3 preponderance of the evidence on its § 523(a)(4) claims. *Grogan v. Garner*, 498 U.S. 279,
4 287, 111 S. Ct. 654, 659 (1991).

5 B. Law

6 The portion of 11 U.S.C. § 523(a)(4) relevant to Plaintiff’s remaining claim against
7 Defendant (Count III) states:

8 (a) A discharge under section 727 . . . of this title does not
9 discharge an individual debtor from any debt –
 (4) for . . . embezzlement

10 While an underlying policy of the Code is to grant a “fresh start” to individual
11 debtors, that “opportunity for a completely unencumbered new beginning [is meant for]
12 the ‘honest but unfortunate debtor’.” *Id.* quoting *Local Loan Co. v. Hunt*, 292 U.S. 234,
13 244, 54 S. Ct, 695, 699 (1934).

14 The parties agree that, in the context of nondischargeability, “embezzlement”
15 requires the presence of three elements:

- 16 1. Property rightfully in the possession of a non-owner;
17 2. Non-owners’ appropriation of the property to a use other than
18 which it was entrusted; and
19 3. Circumstances indicating fraud.

20 *In re Wada*, 210 B.R. 572 (9th Cir. BAP 1997). See also *In re Littleton*, 942 F.2d 551,
21 555 (9th Cir. 1991).

22 In addressing the third *Wada* factor, Retired Bankruptcy Judge Sarah Sharer Curley
23 held that, “[c]ircumstances indicating fraud’ can be situations where the debtor intended
24 to conceal the misappropriation Embezzlement does not require the existence of
25 a fiduciary relationship.” *In re Campbell*, 490 B.R. 390, 402 (Bankr. D. Ariz. 2013)
26 (internal citations omitted).

1 Other courts have held that a debtor's intent to pay back the money she or he does
2 not own, does not negate the intent to defraud. *See Savonarola v. Beran*, 79 B.R. 493, 496
3 (Bankr. N.D. Fla. 1987) (Desire to only temporarily deprive creditor of their property
4 "does not eliminate the inference of intent."); *In re Bevilacqua*, 53 B.R. 331, 334 (Bankr.
5 S.D.N.Y. 1985) (holding that even though Debtor intended to use the funds only
6 temporarily, Plaintiff was deprived of his property and the resulting conversion constitutes
7 embezzlement for purposes of section 523(a)(4)); *Matter of Shuler*, 21 B.R. 643, 644
8 (Bankr. D. Idaho 1982) ("The fact that the intent is to deprive the rightful owner of the
9 funds only temporarily and not permanently . . . does not eliminate the element of intent.
10 For example, in the context of criminal embezzlement, the intention to restore the property
11 is neither a defense to nor negation of the embezzlement. The embezzlement has occurred
12 and the intent to later restore may only be considered in mitigation of punishment.")

13 **VI. Discussion**

14 In its ruling on Plaintiff's Motion for Summary Judgment, this Court previously
15 found that the first two *Wada* elements of embezzlement were satisfied, but ordered the
16 third factor be decided at trial (DE 44). The third and final prong of the *Wada*
17 embezzlement test requires a finding of circumstances indicating fraud. This, however, is
18 not to say the Plaintiff must satisfy all elements of a fraud claim. Of course, a full blown
19 fraud case would be properly pursued under § 523(a)(2).

20 The Court now finds that Debtor attempted to conceal from Plaintiff the fact that
21 he had misappropriated the BCBS insurance proceeds which he knew were owned by
22 Plaintiff. This is evidenced by his answer in the State Court Action where he denied
23 willfully having used the insurance funds belonging to Plaintiff and in his response to the
24 Plaintiff's requests for admission where he denies having spent or otherwise utilized the
25 funds for his own use. At trial in this Court, Debtor now admits to utilizing the BCBS
26 insurance funds for his own personal use and use in his business, instead of rightly paying

1 them to Plaintiff. Although Debtor was forthcoming in this particular proceeding, the
2 Court finds that circumstances indicating fraud exist because Debtor used Plaintiff's
3 money that did not belong to him. The Court finds clear circumstances indicating fraud
4 in Debtor's dealings with Plaintiff.

5 Debtor knew that the money he received from BCBS belonged to Plaintiff. He
6 signed the ASTA acknowledging this fact. He is a chiropractor who knew what signing
7 the ASTA meant. Fully aware of his contractual obligation to pay Plaintiff the money he
8 received from BCBS, Debtor spent the money on his own personal and business expenses.
9 Although Debtor claims he was planning on paying the money back (*See* DE 48), this
10 Court agrees with cases cited above to the effect that such intent does not negate a finding
11 of circumstances indicating fraud. *See Savonarola v. Beran*, 79 B.R. 493, 496 (Bankr.
12 N.D. Fla. 1987); *In re Hoffman*, 70 B.R. 155, 163–64 (Bankr. W.D. Ark. 1986); *In re*
13 *Bevilacqua*, 53 B.R. 331, 334 (Bankr. S.D.N.Y. 1985); *Matter of Shuler*, 21 B.R. 643, 644
14 (Bankr. D. Idaho 1982). Moreover, having carefully observed Debtor at trial and having
15 carefully listened to his testimony, this Court finds Debtor's testimony to not be credible.
16 Rather, the Court finds Debtor never intended to pay any portion of the BCBS funds to
17 Plaintiff.

18 Based on the facts presented at trial, this Court finds circumstances indicating fraud
19 existed in regard to Debtor's actions concerns Plaintiff's health insurance proceeds. The
20 Court further finds the Debtor retained \$149,943.40 of insurance funds owned by Plaintiff.

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23 **VII. Conclusion**

24 The Court finds Plaintiff has sustained its burden of proof concerning Debtor's
25 embezzlement of BCBS insurance proceeds received by Debtor but owned by Plaintiff.
26 All three elements of the *Wada* test have been satisfied by Plaintiff. Plaintiff's claims

1 against Debtor are nondischargeable pursuant to 11 U.S.C. § 523(a)(4). In connection
2 with this claim, Plaintiff has sustained damages in the amount of \$149,953.15.

3 The Court will enter judgment in favor of Plaintiff and against Debtor declaring
4 nondischargeable its claims against Debtor in the amount of \$149,953.15. Plaintiff is
5 hereby directed to lodge a form of judgment consistent with this Court's Under
6 Advisement Order.

7 **DATED AND SIGNED ABOVE.**

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16 COPY of the foregoing mailed by the BNC and/or
17 sent by auto-generated mail to interested parties.
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